

INTERNATIONAL CITY MANAGERS' ASSOCIATION  
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## ADMINISTRATION OF BUSINESS GROSS RECEIPTS TAXES

What are the problems in administering a local gross receipts tax? What are the most effective methods of collecting this tax? What methods of tax enforcement have secured the best results?

The general gross receipts tax is becoming more important in the local revenue structure as broader taxing authority is conferred upon municipalities in more and more states. Approximately 60 municipalities over 10,000 population tax the gross receipts of all business and commercial activities within their limits, 18 of these cities adopting this tax in 1947, according to the 1948 Municipal Year Book. Gross receipts also serve as the basis for many local admissions and utility taxes.

To obtain information on the administration of gross receipts taxes the International City Managers' Association recently sent a questionnaire to the officials of 15 cities: Alhambra, Calif.; Birmingham, Ala.; Columbus, Ga.; Gainesville, Ga.; Harrisburg, Pa.; Kansas City, Mo.; Richmond, Va.; Roanoke, Va.; Roswell, N. M.; Sacramento, Calif.; Seattle, Wash.; Stockton, Calif.; Tampa, Fla.; Vancouver, Wash.; and Wheeling, W. Va. These cities have general business gross receipts taxes although a few tax the gross receipts of public utilities or amusements by means of a special tax. Data supplied by these cities are summarized in this report.

An Effective Local Tax?

The gross receipts tax has several excellent characteristics: (1) it can be administered locally by city officials, (2) with a minimum of regulation, (3) to bring in substantial revenues, (4) at a low cost. It does not involve the accounting problems of the income tax. It is certainly more flexible than the property tax or the flat license fee but it is not as effective a measure of ability to pay as the income tax. The variety of profit margins in different occupations make gross receipts a limited index of ability to pay. The gross receipts tax does reach nonresidents who are engaged in a business, profession, or occupation within the city. In general, it broadens the municipal tax base to spread it over a trading or service area and reaches many who do not reside within the city limits.

The gross receipts tax has been criticized as a tax that is hidden from the taxpaying public if the tax is shifted as is very likely done by retailers and professional people and perhaps to some extent by wholesalers and manufacturers. If the tax should be pyramided--shifted from manufacturer to wholesaler (who adds his bit) and then to the retailer--the consumer may feel the pinch by way of higher prices. But competition with out-of-city firms might prevent any full-scale attempt to shift the tax to the local consumer. As long as the tax rates are kept low, there may be little motivation for passing the tax either on to the consumer or in the reverse direction towards the factors of production. Too heavy a tax may encourage a "flight" of industry from the city, but city officials

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should not let threats of out-migration prevent the adoption of reasonable taxes. Businesses are located where they are for reasons more fundamental than taxes. Efficient public services and effective public relations can overcome many of the objections to the tax.

### Revenues, Cost of Collection, and Number of Employees

Approximately \$10,330,981 in gross receipt tax revenues were collected in the fiscal year ending in 1948 by 14 municipalities included in this survey. The tax revenues ranged from \$36,800 for Roswell up to \$2,591,171 for Kansas City. Small as well as large cities find this tax to be a productive source of needed revenue. In some cities the gross receipts tax returns as much as 15 to 20 per cent of the total general fund revenues.

The cost of collecting gross receipts taxes depends on such factors as the number of taxpayers, the average size of the tax payment, the exemptions and deductions allowed, the rate schedule, salary scale of the city employees, and the variety of activities taxed. Some businesses require little or no auditing to verify the returns, and are much easier to collect taxes from than others, for example, theaters and gasoline stations as compared with professional people or retail-manufacturing combinations, under a tax schedule with different rates for the various categories of business activities. Collection costs range from just under 2 to 9 per cent with most cost ratios falling below 5 per cent ( see table below ). Such ratios are rough indicators at best and are not conclusive.

The taxpayer's cost of compliance ought to be considered. The city levying the tax can reduce the compliance cost if the determination of the amount subject to the tax can be tied in with a federal or state return on other taxes. Seattle and Vancouver overcame businesses' objection to the red tape and paper work by showing that the computation of a state tax automatically gave the base for determining the city tax.

The 14 cities in the table below report from 1 to 25 full-time employees who collect gross receipt taxes, and sometimes other taxes as well. Figures on collections per employee therefore serve no purpose. In the smaller cities the large payments of one or two taxpayers, usually utility companies, may conceal the effort that must be made to collect taxes from small merchants and one-man professional businesses that do not keep accounting records of any sort. Cities like Seattle, Kansas City, Birmingham, and Richmond must retain full-time auditors specializing on taxes in general, or just on the gross receipts tax, in order to check a fair proportion of the returns every year.

### Establishing the Base and Rate

What are Gross Receipts? Gross receipts represent the broadest concept of returns to an enterprise regardless of its nature or source. A retail store, for example, would report all retail sales plus any returns from investments in stocks, bonds, or the sale of property. A common definition of gross receipts is: "Compensation for personal service and the gross receipts of the taxpayer derived from trade, business, commerce, or sales, and the value proceeding or accruing from the sale of tangible property (real or personal) or service, or both, and all receipts by reason of the investment of the capital of the business engaged in, including interest, discounts, rentals, royalties, fees or other emoluments of the cost of property sold, the cost of material used, labor costs, taxes, royalties, interest or discount paid or any other expenses".



## REVENUE, COST OF COLLECTION, AND NUMBER OF EMPLOYEES COLLECTING

City	Population in thousands	1947 Tax Revenue	Cost of Collection	No. Full-Time Employees
Alhambra, California	44	\$ 47,131 <sup>1/2</sup>	\$ 6,000	2 <sup>2/3</sup>
Birmingham, Alabama	268	1,500,000 <sup>2/3</sup>	2%	12 <sup>4/5</sup>
Columbus, Georgia	53	313,147	5,000	1 <sup>1/2</sup>
Gainesville, Georgia	10	....	2,400	1
Harrisburg, Pennsylvania	84	78,404	6,900	2
Kansas City, Missouri	399	2,591,171	33,000	17 <sup>5/8</sup>
Richmond, Virginia	224	2,360,455	29,800	15 <sup>5/8</sup>
Roanoke, Virginia	64	857,714	4,000	1
Roswell, New Mexico	13	36,800	....	...
Sacramento, California	120	270,000	20,000	5
Seattle, Washington	434	1,745,877	72,000	25
Tampa, Florida	108	152,732 <sup>6/8</sup>	5,000	2
Vancouver, Washington	19	155,057	4,000	1
Wheeling, West Virginia	61	200,000	....	...

1. For six months
2. Employees also collected \$17,704 license fees levied on other bases.
3. Estimated
4. Employees also collected \$22,494 flat license fees.
5. Employees also collected \$357,545 motor vehicle revenues and \$210,650 amusement taxes.
6. Also includes revenues from pinball licenses.

The base on which the tax is calculated should be carefully defined in the tax ordinance. Some cities simply state in their ordinances that the gross receipts of all business are subject to the tax. Others like Seattle, Norfolk, and Richmond (Virginia), specify for each broad class of business the base of the tax, sometimes substituting a base other than gross receipts for a particular activity to simplify tax administration. For example, in Seattle retailers and wholesalers use the gross proceeds of their sales without regard to the place of delivery; extractors use the value of the products extracted for sale or commercial use; manufacturers the value of the product produced; and all others use gross income. Norfolk and Richmond require wholesalers to use the amount of their purchases, whether paid for or not during the preceding year, as the basis for computing the tax.

Information Required for Rate Schedule. Perhaps the hardest job is to determine what the tax rate should be for retailers, wholesalers, manufacturers, doctors, lawyers, advertising agencies, etc. In answering this question officials should determine how the city intends to tax the gross receipts and whether the rates are to be regressive, proportional, or progressive in their effect upon the earnings of businesses. The gross receipts tax is essentially a compromise between a rigid flat license fee and a fluctuating net income tax.

The city should collect basic information about the economic character of the community, including the area just beyond the city limits. What and how many of each type of business does the city and shopping area have? Where do the customers come from? What other market areas are available to these customers? What, roughly, are the gross receipts of the various types of businesses in the city and just outside the city limits? What are the average inventory turnover factors for

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the various types of businesses? What are the gross margins or operating ratios for each class of business? City officials can find some of the answers to these questions with the help of local chambers of commerce and trade associations. General information about the revenue, sales, cost of goods sold, cost of operations, and net profits may be found for the different types of business activities in "Statistics of Income", Part 2, of the U. S. Treasury Department, in the publications of the U. S. Department of Commerce, in Moody's and Poor's Manuals, and Dun and Bradstreet.

Types of Tax Rate Structures. There are four general categories of tax rate structures for taxing gross receipts: (1) a flat rate on all gross receipts -- such as 5 per cent; (2) flat license fees plus the flat rates on gross receipts -- such as \$10 plus 5 per cent of the gross receipts; (3) bracketed rate structure with varying flat amounts charged for each higher bracket; (4) bracketed rate structures with a combination of flat amounts and rates charged for each higher bracket.

The first type is easiest to administer and more and more cities are dropping the other types of schedules in favor of this type. The full advantages of the flat rate tax on gross receipts are achieved when businesses are classified according to their activities (see below sections on Tax Rates and Ability to Pay, and Taxing Mixed Businesses). The flat fee plus a flat rate on the gross receipts (No. 2) is very common, and is sometimes used in cities exempting all gross receipts under a specified amount, say \$3,000, leaving the flat fee as the sum to be paid by most taxpayers. It eliminates much of the auditing and checking work by eliminating many of the smaller businesses that do not keep records. Yet a city can lose considerable revenue under such a rate schedule. A variation of method No. 2 is used by Columbus where the flat license fee is graduated according to the number of employees, seating capacity, number of hotel rooms and the like, supplemented by the flat rate tax on gross receipts. The city refunds to the taxpayer that part of his license fee that exceeds his gross receipts tax.

Where the gross receipts are set up in a series of brackets (No. 3 above), a flat license fee is charged for each higher bracket. For example:

Annual Gross Receipts	Amount of Tax
Over \$4,000 up to \$5,000 . . . . .	\$7.00
Over \$5,000 up to \$6,000 . . . . .	\$8.00
Over \$6,000 up to \$7,000 . . . . .	\$9.00

No computation is involved in a tax of this type for all the merchant must do is to find where his gross receipts fall in the schedule, and read across to the fee column. This tax is extremely regressive unless the rate is adjusted sharply upward and the gross receipts brackets are very narrow.

Another bracketed rate structure combines a flat license fee and a varying flat rate with each higher bracket schedule (No. 4):

Annual Gross Receipts	Flat Fee and Tax Rate
Up to \$5,000	\$10 plus 2 mills per \$1,000 of gross receipts
Over \$5,000 up to \$6,000	\$10 plus 1.5 mills per \$1,000 of gross receipts
Over \$6,000 up to \$7,000	\$10 plus 1 mill per \$1,000 of gross receipts

This type of rate schedule is clearly regressive since the taxpayer earning \$5,500 pays \$10 plus  $1\frac{1}{2}$  per cent of \$5,500 while the taxpayer earning \$6,500 pays \$10 plus only 1 per cent of \$6,500. Another variation of this schedule, also regressive, is to apply the tax rate to that part of the gross receipts falling in each bracket. The taxpayer earning \$5,500 pays 2 per cent on all receipts up to and including \$5,000 and  $1\frac{1}{2}$  per cent on all receipts over \$5,000. This tax



schedule is particularly difficult for the taxpayer who must multiply several times with different rates to compute his tax payment. Upward adjustments in the tax rates can eliminate the regressive character of this type of a schedule.

Another disadvantage of the bracketed type of rate structure is that each type of business or occupation will fight for schedules that require the lowest tax payment. Any city using the bracketed rate schedule must decide how many levels of brackets should be used, how wide each bracket should be, and what the bracket should be for each type of business activity. Some cities unfortunately halt the bracketing at a certain point and charge a flat license fee against all gross receipts above the top level. This type of tax is extremely regressive since the business concerns with the greatest gross receipts then pay only nominal sums. The bracketed license schedule should be avoided in favor of the flat rate on all gross receipts.

Tax Rates and Ability to Pay. Cities should keep their rate structures as simple as possible and yet some recognition should be given to "ability to pay". A rate structure that charges a certain per cent of the gross receipts has commendable simplicity but the same rate on all business may be just as unfair as some of the regressive rate schedules cited above (Nos. 2, 3, and 4). It simply is not reasonable to conclude that a single tax rate schedule treats all businesses alike. Some allowance must be made for variations in the relative profitability of different types of enterprises. Unless such an allowance is made in the tax rates, then some business incapable of absorbing the tax will suffer unfairly in the competitive arena or overtly push the tax on to someone else--the consumer and/or its suppliers.

A step in the direction of ability to pay is the classified gross receipts tax, with business enterprises arranged by type of activity, that is, retailers, wholesalers, manufacturers, contractors, professional services, service trades, etc. A growing number of cities are taxing these classes of activities at different tax rates. The usual criteria for classifying businesses in this manner are that their margins of profit are different, sellers of tangible goods employ different percentages of markup, and some firms must meet competition of business elsewhere that probably go untaxed. These reasons are satisfactory, but they are not sufficient to support specific tax rates in a particular ordinance.

Before deciding on the tax rates, the city should analyze the profit margins of the enterprises to come under the tax. Some criteria should be gathered to support the variations in tax rates. Most cities tax retailers at double the rate levied on wholesalers. This may be perfectly fair, but what evidence do these cities have for their rates? City officials might obtain from local businesses information on gross margins and the ratio of cost of operation to total receipts. Some local businessmen might shy at providing net income data or supplying their federal income tax returns--but not at supplying data on gross margins. Deriving average profit ratios for each class of activity, the city would have some evidence for arranging its tax rates on the basis of ability to pay. Reference was made to sources of information earlier in the section on Information Required for Rate Schedules.

Tax Rates in Effect. Cities adopting general gross receipts taxes on all businesses usually levy low rates which range from 1/100 of 1 per cent up to 2 per cent. A few cities with general gross receipt taxes levy higher rates on public utilities, from 2 to 5 per cent. Cities that levy gross receipt taxes only on public utilities or amusement enterprises tax at rates from 2 to 10 per cent. Columbus, Ga., for example, taxes the electric and gas utility at 3 per cent on

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domestic and commercial sales, insurance premiums at 2 per cent, but all other businesses at rates from 1/10 of 1 per cent up to 1 per cent. The low rates of general gross receipts taxes are exemplified by the Seattle tax, with rates of 1/10 of 1 per cent on extractors, retailers, and most wholesalers, and 1/100 of 1 per cent on grain wholesalers. Norfolk, Va., taxes retailers at 3/10 of 1 per cent, professional services at 6/10 and contractors and wholesalers at 15/100 of 1 per cent. Pittsburgh, Harrisburg, Clairton, McKeesport, and other Pennsylvania cities levy mercantile license taxes ranging from 1 to 5 mills on retailers and from  $\frac{1}{2}$  to  $2\frac{1}{2}$  mills on wholesalers.

### Tax Enforcement

Once the tax ordinance is adopted, the municipality must establish an enforcement procedure to encourage payment of the correct amount of tax, and to discourage tax dodging, miscalculations, erroneous reporting, and falsified returns. Many city officials do not have any experience in administering a tax that depends so much on the taxpayer's accounting records and is open to fraudulent reporting. Property taxes, flat license fees, water bills, and auto licenses, do not offer much experience for administering the gross receipts tax. Field audits, supplementary city records, and published directories, penalties and interest payments, seizure of property and arbitrary assessments of the tax are the six principal weapons that are employed by city officials in administering this tax.

Field Audits. The field audit is perhaps the administrator's best weapon to insure the right amount of tax payment. Only six of the 15 municipalities surveyed conduct field audits of the returns supplied by the taxpayer. These cities are: Kansas City, Seattle, Alhambra, Richmond, Stockton, and Columbus, while Vancouver intends to set up such a procedure. In Alhambra the field license inspector may call on the taxpayer to see his federal income tax return in case there is reason to doubt his report. In Richmond the tax auditor may review not only the income tax return but also accounting records for the previous four-year period. Stockton compares the taxpayers' license tax statement with both the federal income tax return and the city sales tax report.

Certainly any administrator of a gross receipts tax should have authority to examine the books, papers, and records of any taxpayer subject to this particular tax. Such authority should not only allow the tax administrator to examine the records on the taxpayer's premises but also to compel the production of any records as well as persons in public hearings. These strong measures may rarely be used but sometimes the mere threat of an audit will bring a corrected tax return. Walking quietly with a big stick may prove to be the best administrative technique in most cases.

Using Public Records to Check the Tax Payment. Tax officials should have an up-to-date list of all commercial and professional establishments in the city. The job of maintaining such a list is simplified if the tax ordinance requires a small flat license fee to conduct a business in the city in addition to the gross receipts tax. Other methods include the use of the water, building, and street department records as in Alhambra, or the health, plumbing, electrical, and building records as in Sacramento. Stockton uses the records of its inspection departments and also regularly secures lists of new subscribers from the telephone company.

Seattle checks the county auditor's recordings of new businesses established in the area and also makes a canvass of the city with its field men.



Kansas City compares its list of taxpayers with all published directories and also with the records of the city assessor. Furthermore, in Kansas City no license is issued unless the personal property tax is paid. Vancouver also makes a sight inspection, checks newspaper ads and the telephone directory, and obtains information from the chamber of commerce and the state tax office. Wheeling similarly checks on new firms with the local board of trade and also with the state license department. Harrisburg obtains a list of all enterprises within the city from its state unemployment insurance reports.

Penalties and Interest. Most cities provide for penalties and interest on any tax payments that are either delinquent or intentionally miscalculated. In some cases the city also applies a penalty if the field auditor discovers any deficiency in the tax payment. For example, in Birmingham all licenses are due on January 1 with a 15 per cent penalty applied on April 1. A 25 per cent penalty applies in any deficiency discovered by the auditors. Sacramento requires that all licenses be paid in advance with a penalty of 10 per cent added after 15 days' delinquency. Penalties and interest encourage prompt tax payments. The tax collector, however, should have authority to waive any penalties if the overdue or the miscalculated payment is covered by a situation beyond the control of the taxpayer.

Collecting Delinquent Accounts. When the taxpayer defaults on his tax payment, the city should have a well-defined procedure for collection of the delinquent account. Sometimes a speedy procedure is desirable whereby an administrative official may issue a warrant authorizing seizure of the taxpayer's property to insure payment of the tax. Unless transient enterprises are otherwise licensed, quick seizure is almost an administrative necessity. The tangible assets may include only cash on hand and a small amount of personal property.

Usually a court order is necessary in order to seize the property. Seattle, for example, cancels the delinquent taxpayer's business license and collects the unpaid license fees, taxes, and penalty by means of a court order. In a number of cities the city collector turns his complaint over to the city attorney who files suit in behalf of the municipality. If a court order may be obtained with reasonable dispatch, and also if the taxpayer cannot flee the jurisdiction of the municipality in the meantime, then certainly a court order ought to be obtained before the property is seized. Advance payments of an estimated tax, as is done for certain athletic contest under admissions tax ordinances, or frequent tax payment dates should enable the city to reduce the amount of delinquency.

Arbitrary Assessment of Tax. Sometimes a taxpayer refuses to file a tax return, or more often will not divulge information needed to confirm his financial report. In such cases the tax collector ought to be able to make an arbitrary assessment of the tax due, based on evidence as can be obtained. Arbitrary assessment has long been employed for property taxation by assessors if information on true value is not available. Twelve of the 15 reporting municipalities indicated that they can make arbitrary assessments of the tax in case the taxpayer willfully fails to file a return. But an arbitrary assessment usually must be based upon the records of the taxpayer. These cities are Tampa, Birmingham, Alhambra, Roanoke, Columbus, Roswell, Stockton, Seattle, Kansas City, Sacramento, Richmond, and Harrisburg. In Kansas City such assessments are made on the basis of audits by the license division if the taxpayer does not voluntarily furnish information.

The provision of the Beckley, West Virginia, gross sales tax ordinance is typical: "If any person fails or refuses to make a return either in whole or in part, or if the city recorder has reasonable ground to believe that any return

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made is so deficient as not to form the basis of a satisfactory assessment of the tax, he may proceed as he deems best to obtain information on which to base the assessment of the tax. The city recorder may by himself or his duly appointed agent, make an examination of the books, records, and papers, and audit the accounts of any such person, and may take the evidence and administer it by himself or his agent, on oath, of any person who he may believe may be in possession of any relevant information. As soon as possible after procuring such information as he may be able to obtain as to any person failing or refusing to make a return, the city recorder shall proceed to assess the tax and notify the person assessed of the amount of the tax. The assessment of the tax by the city recorder shall be final as to any person who refused to make a return."

The tax ordinance might require business concerns to retain their accounting records and forms for a period of time, say five years, to permit auditing of past tax returns in the event a deficiency assessment is to be made. Seattle requires its taxpayers to retain their notes, books and records for five years.

#### Other Administrative Problems

Exemptions. Theoretically there should be no exemptions from the gross receipts tax except governmental agencies. But charitable, religious, and other nonprofit enterprises usually are exempt from the tax on the same grounds that they are exempt from all other taxes. In some cities particular enterprises such as commercial amusements are exempt from the gross receipts tax because they are subject to their own special taxes. Some cities specify the activities that are subject to the tax and make no reference whatever to the activities that are exempt from the tax. It is desirable that any exempt activities be named in the ordinance.

All exempt enterprises should be registered to make sure that no taxable activity escapes from the tax or that the exempt activity has not changed its status. Sometimes a religious or charitable enterprise becomes the owner of property that is not an integral part of the exempt activity so that a tax might be paid on the non-exempt portion of its revenue. Seattle is one of the few cities that maintains a list of exempt enterprises which of course serves as a basis for a review of any exemptions granted. Birmingham, Kansas City, Richmond, Sacramento, Seattle, Stockton, and Vancouver recheck the activities of all exempt enterprises to confirm or deny a continued exemption. Each and every activity exempt from the tax should bear the burden of proving that its function is exempt under the terms of the ordinance. The provision allowing exemption from the tax ought to be strictly construed.

Deductions Allowed. A few cities specifically allow the taxpayer certain deductions before he computes his tax payment. Most cities do not by ordinance stipulate any permissible deductions yet their officials must argue with taxpayers who hotly claim the right to reduce their gross receipts before applying the tax rate. A few rules might help. The regulations of the Philadelphia school district permit the following deductions:

1. Refunds, credits, or allowances given by a vendor or dealer to a purchaser on account of defects in goods, wares, and merchandise sold or on account of goods, wares and merchandise returned; may be deducted from the amount of the "gross volume of business" of the vendor or dealer.
2. Trade discounts allowed to customers may be deducted from "gross volume of business" if they are in the nature of (1) discounts deducted on the face of the bill as a medium of adjusting the list price, and (2) discounts unconditionally



deducted by customers upon settlement of their bill and allowed as a matter of the established custom of the trade or line of business without regard to the due date of such bills or the form or terms in which such discounts are described or stated on bills of invoice.

3. The following federal and state excise taxes may be excluded from the gross volume of business provided such taxes are separately stated on the evidence of charge or sale: Federal tax on admission and dues, federal retailers excise tax on jewelry, furs, and fur articles, toilet preparations, and luggage, Pennsylvania liquid fuel tax, and the Philadelphia amusement tax.

4. Property traded in. In the case of trade in transactions in which goods are sold and allowance is made for other property which is traded in and is accepted by the vendor or dealer as part payment of the property sold, the allowance made for the property traded in shall not be deducted from the selling price of the property sold in computing gross receipts upon which the tax is based.

5. Property repossessed. Where goods are repossessed by the seller and the repossessed property is subsequently sold, the gross receipts from such sales are to be included in the gross volume of business only to the extent by which the amount of the sale exceeds the balance due on the original sale at the time of repossession. No deductions from gross receipts may be taken at the time of repossession for any unpaid balance due.

Seattle and Vancouver allow the taxpayer to deduct credit losses actually sustained by the taxpayer if the accounting records are kept on an accrual basis. None of the municipalities studied allow sales to governmental agencies to be deducted despite the tax free status of the buying agency. On the other hand, some cities grant a flat deduction from the tax due, such as the \$12.50 deduction allowed by Beckley, W. Va., or allow the taxpayer to deduct \$1,200 from his gross receipts before he computes his tax due, as in Princeton, W. Va. Theoretically there is no justification for flat tax deductions, or flat deductions from the gross receipts of all taxpayers. If the city intends to exempt all businesses making less than \$1,200 each year, the ordinance can specify such an exemption.

Taxing Out-of-City Sales. Most cities specifically exempt interstate sales or sales in "interstate commerce". But there is a large area of out-of-city sales that may be taxed without placing an undue burden upon interstate commerce. Naturally some taxpayers try to escape taxation on part of their gross receipts, claiming that it is "interstate commerce", draping the flag around themselves, and relying on the gullibility of the local official to bluff the thing through. The mercantile license tax regulations of the Philadelphia school district may help the city officials who have not developed their own rules:

1. Shipment from Philadelphia by vendor or dealer. Receipts are excluded if the Philadelphia vendor or dealer, as a necessary incident to the contract of sale, agrees to and does deliver the property to a purchaser outside of Pennsylvania, or delivers the property to a common carrier consigned to the purchaser at a point outside Pennsylvania.

2. Shipment into Pennsylvania from out of state factory or vendor or dealer. Receipts are excluded if, by the terms of the contract of sale or the established practice of doing business, the vendor or dealer is required to make delivery by transporting or shipping the property from his factory or warehouse situated outside Pennsylvania directly to the purchaser at a point within Pennsylvania.

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3. Shipment into Pennsylvania from other out of state factory of third party. Receipts are included if the Philadelphia vendor or dealer causes delivery to be made at a point in Pennsylvania from an out of state source of supply owned and operated by a third party (one from whom the vendor buys). For example, if a dealer in Philadelphia causes an automobile to be delivered directly to the buyer from the factory of the manufacturer in Detroit, the receipts are included in the dealer's gross volume of business on which the tax is based.

4. Delivery from out of state factory of vendor or dealer via his Pennsylvania office. Receipts are included if the property is shipped from the out of state factory or warehouse of a Philadelphia vendor or dealer to his (the vendor's or dealer's) place of business in Pennsylvania from which point the goods are delivered to the purchaser.

5. Sale and delivery in Philadelphia. Receipts are included in the sale of a Philadelphia vendor or dealer to customers located outside Pennsylvania where the property is delivered directly to the purchaser or his agent within Pennsylvania notwithstanding the fact that the purchaser or agent intends to, and later does, transport the property to a point outside the state.

Sometimes city officials must set up rules to guide the taxpayer in separating the nontaxable receipts from certain out-of-city sales from the total gross receipts. The New York State Tax Commission has prepared a model gross receipts tax ordinance that includes a provision authorizing the city official to set up allocation formulas:

"Where a receipt in its entirety cannot be subjected to the tax imposed by this local law, by reason of the provisions of the Constitution of the United States or any other provision of law, the \_\_\_\_\_ shall establish rules and regulations or methods of allocation and evaluation to the end that only that part of such receipt which is property attributable and allocable to the doing of business in this city shall be taxed hereunder. The \_\_\_\_\_ may make such allocation, with due regard to the nature of the business concerned, on the basis of mileage, division of the receipt according to the number of jurisdictions in which it may be taxed, the ratio of the value of the property or assets of the taxpayer owned and situated in the city to the total property owned or assets of the taxpayer wherever owned and situated or any other method or methods of allocation calculated to effect a fair and proper allocation in accordance with the purposes of this subdivision".

As a very minimum the tax ordinance should require the taxpayer making out-of-city sales to retain all records pertaining to the sales and produce them upon demand to substantiate his plea for the deduction of that part of his receipts.

Tax Avoidance. Firms going out of business should not be permitted to avoid payment of any tax due. One method to prevent or reduce losses from this source is to require tax payments quarterly. Wheeling, W. Va., relies on the beat patrolmen to observe and report any fire sales and closing-out sales. Seattle depends on its field men to follow-up the delinquent notices. In the cases of firms selling out to another organization Kansas City, Mo., collects the license tax from the successor. Some cities require the taxpayer to make a payment in advance as is done in Harrisburg where a new business establishment must pay an assessment estimated on the basis of the first month's business.

Taxing Mixed Businesses. Cities are gradually swinging toward a classified gross receipts tax, with different tax rates for various classes of business activity. Some cities classify all business according to whether they are retail,



wholesale, construction, amusements, service trade, professional service, and the like, and levy different tax rates on each group. The tax official must not only determine what type of activity the taxpayer is carrying on, but also in the case of a "mixed business", such as a retailer-wholesaler combination, decide what share of the gross receipts is attributable to each activity.

To tax fairly the gross receipts of a retailer-wholesaler combination, or any other type of "mixed business", the city (1) can require the separation of the gross receipts according to each activity and levy the correct rate on each portion, or (2) combine all of the gross receipts into a lump sum and levy the rate applicable to the bulk of the business. Of the two methods, the first is to be preferred. An undesirable variation of the second method occurs where the city taxes the gross receipts of all activities lumped together at the lowest rate available to the business. In contrast, Norfolk, Va., permits a wholesaler conducting a retail business in part to be taxed for all of his receipts at the higher rates provided for retailers. Whatever method is used, the city tax staff should audit the taxpayer's books and records to verify the percentage of receipts coming from each source.

Ten cities covered in this survey depend upon an interview with the taxpayer or an inspection of his premises to ascertain the type of business. Seattle, for example, requires the taxpayer to make a declaration which is examined by a tax official who inspects the record. Inspections also are made at Kansas City and Roswell while the information is obtained by interview in Gainesville, Sacramento, and Stockton.

Frequency of Tax Payment. Most cities provide for quarterly payments of the tax, some cities require payment twice a year, and a few provide for a single payment each year. Bi-monthly payments are required by Seattle and Vancouver to conform with the state schedule on sales tax payments. Sacramento requires retailers to pay quarterly and all professional businesses to pay annually. Columbus requires its flat license fee to be paid by February 15 with the payments based on gross receipts payable every quarter. Some cities authorize the city collector to require immediate payment if he suspects that the taxpayer is going out of business and intends to avoid the tax by quick disposal of his goods.

Refunds of Protested Tax Payments. Sometimes the taxpayer makes an overpayment of the tax or may make a payment under protest, demanding that the city refund the tax to him. The city should set up a well-defined procedure that the taxpayer making a payment under protest should follow in order to obtain the refund. Kansas City requires a clear proof of the claim of overpayment, demanding the presentation of federal and state income tax returns, state sales tax returns, original accounting records, or at the option of the commissioner of taxes, the taxpayer must submit to an audit. If the taxpayer did not pay enough, then he is subject to penalties prescribed by the ordinance. In New York City the controller holds hearings and upon his determination may order the treasurer to refund the overpayment. But in any case the tax must be paid first. Very few cities, perhaps, take the precaution to set aside the protested payment unless there is a substantial sum involved. Under its local law, New York City must establish a reserve to provide for the repayment of protested tax payments.

Protests Against the Tax. Protests against the gross receipts tax can be expected particularly in the case of a city adopting this tax for the first time. Such protests will die out as the tax becomes generally accepted and as its administration improves. Alhambra, Sacramento, and Richmond received most complaints from professional groups and Alhambra from the owners of rental property.

(Over)



Some doctors, attorneys, and other professional groups licensed by the state feel that their state license frees them from any taxation by the municipality where they set up an office. Attorneys doing business in Los Angeles claimed such an exemption but the city successfully disputed this contention in the California district court of appeals which held that the city can levy a tax upon the business of practicing law.

It is common for one group of business concerns to protest that they are discriminated against, that their tax should be lower than that of another group. This occurs even in the cities that have a uniform tax rate for all types of businesses. In the first case certain business concerns will feel that they should be differentiated from other types of activities while in the second case they probably feel that the tax rate is not low enough. Columbus, Ga., for example, received protests from automobile dealers and wholesale grocers who objected to the rates and received a reduction from the city council. Large merchants in that city also objected to the method of taxation but no action was taken. In Kansas City, Mo., businessmen are reluctant to report all of their receipts during periods of high business volume, particularly wholesalers and manufacturers doing business both inside and outside of the state. To overcome their objections, Kansas City bases the tax only on the volume done within the state of Missouri.

Where the gross receipts tax is new to the city, some businessmen may object to the red tape and form-filling entailed in paying the tax. A few will even say that they must hire accountants to pay their taxes. The city can overcome such complaints by showing the businessman how he can rely on other tax records to complete his city tax return. For example, in some states the definition of receipts or sales under the state sales tax automatically provides the tax base for the city's tax.

Newspapers may also protest paying taxes based on their gross receipts, as occurred in Tampa, Fla., as an infringement on the freedom of the press. The United States Supreme Court, on October 13, 1947, refused to review the decision of the Florida Supreme Court upholding a city license tax on the gross receipts from all sales and advertising of newspapers and other periodicals ( Tampa Times Co. vs. City of Tampa ).

Generally litigation should be avoided if some reasonable agreement can be reached with the taxpayer. Of course, no taxpayer should expect the city to grant some special benefit at the expense of other taxpayers. If it is necessary to bring suit in court to compel payment of the tax, the city should be extremely careful in stating its case, especially if the tax has never had a court review previously.

Note: Information on cities that levy gross receipts taxes on businesses and on utilities is published annually in "The Municipal Year Book" (see, for example, ppl79 and 185 of the 1948 edition). MIS subscribers may obtain on request loan copies of gross receipt tax ordinances and regulations, and information on operating ratios of various businesses.



MANAGEMENT INFORMATION SERVICE

1313 East 60th Street, Chicago

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